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February 24, 2005

To: Supervisor Gloria Molina, Chair
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From: David E. Janssen
Chief Administrative Officer

SACRAMENTO UPDATE

LEGISLATIVE ANALYST'S OFFICE (LAO) REPORT: ANALYSIS OF THE BUDGET BILL

Today, the LAO released the second and more detailed analysis of the Governor's Budget proposal. The February 22, 2005 Sacramento Update provided a summary of the LAO's first report, The 2005-06 Budget: Perspectives and Issues, which contained their analysis of the budget's economic assumptions, revenue projections, the elements of the Governor's budget solution, and the major issues they posed for the Legislature. Today's LAO report is a detailed analysis of the entire budget, including their findings and recommendations on the proposed funding levels. As such, it is the starting point for the Legislature's deliberations on the State Budget. A copy of the full report is available at www.lao.ca.gov. The LAO's Highlights of the 2005-06 Analysis is attached.

K-12 spending constitutes 32 percent of the State spending. Given the current political controversy over whether the Governor's budget, which continues the suspension of the Proposition 98 guarantee, really reduces education spending by over \$2 billion, the Legislature's ultimate resolution of this issue could have a significant impact on other areas of the budget that fund county programs. Consequently, the LAO's position on this issue is of special interest. The LAO appears to be in basic agreement with the Governor's recommended level of funding in the current year and the budget year, though its rationale for the budget year level differs from the Governor's. Most importantly, the LAO does not recommend an increase in the base level of funding for K-12 schools in either year. However, they do recommend against shifting the State's

contribution toward education pensions to school districts and recommend instead, that if the Legislature decides to provide additional funding beyond the level the LAO believes is adequate to maintain current levels of service, it should do so by beginning to reduce the \$3.6 billion it has borrowed from schools in recent years.

Higher education accounts for approximately 11 percent of State spending. The Governor's recommendations in this area adhere to the "compact" he developed with the higher education systems last year, including annual adjustments for enrollments, fees and base funding increases through FY 2010-11. The LAO recommends that the Legislature disregard the compact and instead fund the systems based on actual enrollments, utilize the fee increases to reduce General Fund support, and increase community college fees beyond the level recommended by the Governor, further reducing the need for General Fund support. The overall impact, if adopted by the Legislature, would be to free up monies for other areas of the budget.

This Update will focus on the items of interest to the County in the Governor's Budget that were identified in our January 10, 2005 Sacramento Update.

Health

Medi-Cal. Expenditures are projected to be \$34.1 billion in FY 2005-06, including \$12.9 billion General Fund, an increase of \$981.7 million, or 8.2 percent. **The LAO indicates that the Budget's overall estimate for the Medi-Cal caseload is reasonable, but that it could be significantly higher or lower than budgeted due to the offsetting effects of various policy changes. The LAO recommends that the Legislature recognize about \$294 million in Medi-Cal revenues from "quality improvement fees" that have not been counted as State revenues in the Governor's budget, and suggests another \$100 million could be gained by extending the fee to hospitals.**

Medi-Cal Program Redesign. Recommends \$12.3 million net General Fund savings from redesigning Medi-Cal including:

- a projected savings of \$24.8 million from capping the Medi-Cal dental benefit package at \$1,000 annually for adults.
- \$3.4 million to expand use of managed care for families and children in up to 13 additional counties and shift aged, blind and disabled participants into managed care plans.
- \$6.8 million to establish monthly premiums for individuals with incomes above the poverty level and for seniors and persons with disabilities above the SSI/SSP level.

- \$.98 million to streamline enrollment for children through processing by the Single Point of Entry vendor instead of counties.
- \$.61 million for County performance standards monitoring.

Overall, the LAO finds that the Governor's proposals for Medi-Cal Redesign are conceptually sound, but that the Legislature needs more information about some aspects of the package and that refinements are warranted. The LAO recommends: 1) reducing the item by \$602,000; 2) withholding a total of \$29 million provided to the California Department of Health Services and to Los Angeles County for administrative funding until the Legislature receives monitoring reports on the Los Angeles County Medicaid Demonstration Project; and 3) directing the California Department of Health Services to report at budget hearings on the fiscal impact on Los Angeles County of the proposed hospital financial waiver and Medi-Cal redesign.

The Proposed Budget indicates that the Administration is working on an approach to respond to Federal criticism of the way safety net hospitals are financed under Medi-Cal but provides no specifics on the plan. **The LAO notes that the Administration is negotiating with the Federal government for a comprehensive redesign of hospital financing as part of the Medi-Cal redesign package.** The LAO indicates that this proposal could help preserve the financial stability of public hospitals, but that it also raises some significant fiscal and policy issues including the use of Intergovernmental transfers.

The LAO additionally notes that the new Medicare drug benefit will probably result in a significant net cost to the Medi-Cal Program over the next several years.

Expanding Health Insurance Coverage for Children.

- Proposes \$5.9 million in General Fund and \$8.6 million in matching Federal funds to re-establish application assistance fees.
- Includes \$5.6 million to establish Medi-Cal/Healthy Families Bridge Performance Standards to ensure that counties comply with the requirement to forward applications to the Healthy Families Program for children who are no longer eligible for Medi-Cal.
- Provides \$.49 million in FY 2004-05 and \$.91 million in FY 2005-06 from the First 5 California Children and Families Commission as State share to obtain Federal financial participation for technical assistance to counties providing local, low-cost health coverage to children not eligible for Medi-Cal or Healthy Families.

- Proposes to update the joint Medi-Cal/Healthy Families application form to make it easier for parents to complete, including an authorization form to release information to certified application assistants.

The LAO does not provide any comments or recommendations.

California Obesity Initiative. Includes \$6 million General Fund for a comprehensive obesity prevention program to promote healthy eating, regular physical activity, and responsible choices by individuals. **The LAO recommends that the California Obesity Initiative be reduced by \$5.8 million because it is premature before an assessment of existing State efforts is complete and because it does not take full advantage of available alternative funding sources.**

Prescription Drugs for the Uninsured. Includes \$4 million General Fund to implement the California Rx (Cal Rx) Program to provide prescription drugs for an estimated 4 million Californians with ongoing prescription drug needs. **The LAO does not provide any comments or recommendations.**

Streamlining Hospital Construction Review. The Administration will sponsor legislation to allow hospitals to contract with an independent plan reviewer for large hospital construction projects. **The LAO does not provide any comments or recommendations.**

Public Health. State expenditures for all public health programs and State administration total \$3.5 billion (\$703 million General Fund), an increase of \$53.5 million in general funds, or 8.2 percent. **The LAO recommends that the Legislature begin to address the long-term issues posed by the present structure of Proposition 99 and seek the approval of voters to restructure Proposition 99 to enable the State to focus funding more effectively as tobacco revenues continue to decline.**

Newborn Screening Program Expansion. Includes \$15 million from the Genetic Disease Testing Fund to expand newborn screening for an additional 37 treatable genetic diseases. **The LAO does not provide any comments or recommendations.**

Bioterrorism Prevention and Preparedness. Includes \$108.6 million in Federal funds to support California's public health system's capacity to respond to bioterrorism, outbreaks of infectious diseases, and other public health threats. **The LAO does not provide any comments or recommendations.**

Children's Medical Services. Includes \$243.7 million, an increase of \$22.7 million above the FY 2004-05 Budget. **The LAO does not provide any comments or recommendations.**

HIV/AIDS Treatment and Prevention. Includes approximately \$381 million for the HIV/AIDS Treatment and Prevention Program administered by the Office of AIDS, an increase of \$20.1 million. **The LAO does not provide any comments or recommendations.**

Additional Medi-Cal Pharmacy Rebates. Assumes \$20 million in General Fund savings in recently negotiated rebates for heartburn medication. **The LAO does not provide any comments or recommendations.**

Maximize Federal Funds for Prenatal Care. Proposes \$191 million in General Fund savings reflecting accessing Federal funding for prenatal care provided in Medi-Cal. An additional \$51 million General Fund savings is proposed for the Access for Infants and Mothers (AIM) Program. **The LAO recommends that the Legislature approve the Administration's proposal and recommends its expansion to include incarcerated women. In addition, it recommends coverage of low-income pregnant women in the Healthy Families Program.**

AIDS Drug Assistance Program (ADAP) Rebates. Proposes \$8.8 million in General Fund savings related to higher-than-anticipated collections of drug manufacturer rebates. **The LAO is withholding a recommendation on funding for local assistance for ADAP until more information is available on the State's Federal allocation and the supplemental rebates, but recommends approval of additional staff to negotiate better price discounts with drug manufacturers.**

Office of Bi-national Border Health. Eliminates \$694,000 in General Fund support; \$500,000 in Federal funds remains to support the office's mission. **The LAO does not provide any comments or recommendations.**

Addressing California's Nursing Shortage. Proposes meeting the forecast demand for more registered nurses between 2000 and 2010 by increasing the number of persons educated in California Community Colleges, institutions of higher education, and nontraditional education environments using Workforce Investment Act (WIA) funds. In FY 2004-05 and FY 2005-06 the Administration proposes allocating a combined total of \$35.6 million in WIA funds for the training of nurses and other health care workers. **The LAO does not provide any comments or recommendations.**

Mental Health

AB 3632 Mental Health Services. The LAO recommends permanently shifting responsibility for mental health services provided to emotionally disturbed students to Education and providing an additional \$43 million in funding for a total of \$143 million.

Proposition 63 - Mental Health Services Act (MHSA). The State Department of Mental Health will present a detailed resource needs assessment for implementation of the MHSA for both FY 2004-05 and FY 2005-06 in the May Revision. **Because uncertainty regarding some provisions in Proposition 63 could complicate implementation and cause problems for future State budgets, the LAO recommends that the Legislature add new provisions to the Mental Health Services Act to clarify major ambiguities in the law.**

Community Mental Health Services - Early and Periodic Screening, Diagnosis, and Treatment Program (EPSDT). Of the \$1.8 billion included in the Governor's Budget for community mental health services, a net increase of \$86.3 million, \$801.2 million is budgeted for EPSDT, an increase of \$76.7 million to cover projected claims. **The LAO does not provide any comments or recommendations.**

Sexually Violent Predators (SVP). Proposes a \$9.2 million General Fund savings for the State hospitals for FY 2005-06 by keeping pre-commitment SVPs in local custody until they are committed by the courts as SVPs, and by transferring existing pre-commitment SVPs in State hospitals to local custody. **The LAO does not provide any comments or recommendations.**

SVP Treatment Restructuring. Proposes a \$6 million General Fund savings for the State Hospitals for FY 2005-06, growing to \$11 million in FY 2006-07, by restructuring supervision and treatment services provided by State hospitals to SVPs. **The LAO does not provide any comments or recommendations.**

Social Services

CalWORKs Employment Services. Maintains an augmentation of \$191.9 million for employment services provided in FY 2004-05 and FY 2005-06, but deletes the one-time legislative augmentation for CalWORKs employment services provided in FY 2004-05, for savings of \$50 million. **The LAO does not provide any recommendations.**

CalWORKs Grants. Proposes to save \$212.3 million in FY 2005-06, and annually thereafter, by reducing grants by 6.5 percent. **The LAO only recommends that funding for CalWORKs grants be reduced by \$17.4 million in FY 2005-06 because the caseload is overstated.**

CalWORKs Cost-of-Living Adjustment (COLA). Proposes to save \$163.8 million in FY 2005-06 and thereafter by permanently eliminating the COLA. **The LAO does not provide any recommendations.**

CalWORKs Work Requirements. Proposes to save \$12 million because of the impact of the CalWORKs reforms enacted in FY 2004-05 which strengthened work requirements. **The LAO does not provide any recommendations.**

CalWORKs Earned Income Disregard. Proposes to save \$79.5 million in FY 2005-06 and \$109.3 million annually thereafter by reducing the earned income disregard from the current \$225 and 50 percent of the remaining earned income to \$200 and 40 percent of remaining income. **The LAO does not provide any recommendations on this issue, but presents two alternatives to the Governor's proposal: 1) disregard all income at a constant percentage rate; or 2) disregard more income at higher earnings.** The LAO notes that these approaches would likely increase the work incentive for CalWORKs recipients, but result in lower budget savings.

CalWORKs Pay for Performance Proposal. Proposes to save \$22.2 million in FY 2005-06 by implementing a new incentive system that bases a portion of the counties' single allocation for administration and employment services on specific outcomes of CalWORKs clients in each county. **The LAO does not provide any recommendations, but indicates that the proposed hold back is likely to be disruptive, could compound the existing problem of unspent funds, and may leave low performing counties with insufficient funds to improve their performance.** The LAO does, however, believe that the Legislature should consider adding county performance measures.

CalWORKs Child Care. Proposes funding of \$461.5 million including savings of \$50.9 million associated with cases reaching the CalWORKs 60-month time limit. Also included is a budget reduction of \$62.6 million due to a proposed change in reimbursements. **The LAO recommends delaying the shift of the Stage 3 program to Alternative Payment child care until counties have created centralized waiting lists, and recommends placing current CalWORKs child care on the waiting lists based upon the date that they first had earned income in the program.**

Adjustments to CalWORKs Employment Services and Administration Funding. Proposes to save \$42.9 million by modifying the past practice of not adjusting current year funding when updated estimates would result in lower costs. **The LAO does not provide any recommendations.**

Tribal Temporary Assistance for Needy Families (TANF) Expenditures. Proposes to save \$5 million by reducing the amount of State funding provided to the tribal entities in FY 2004-05 to reflect an anticipated decline in programmatic expenditures. **The LAO does not provide any recommendations.**

Statewide Fingerprint Imaging System. Proposes \$8.0 million for maintenance and operation, a \$95,000 increase. **The LAO does not provide any recommendations.**

Los Angeles Eligibility, Automated Determination, Evaluation and Reporting (LEADER) System. Includes \$13.4 million for maintenance and operation of the

LEADER System, which represents a \$1 million reduction for planning costs. **The LAO does not provide any recommendations.**

Reduce State Participation in In-Home Supportive Services (IHSS). Proposes to save \$152.1 million General Fund in FY 2005-06 and \$216.8 million thereafter, by reducing the maximum level of IHSS provider wages and benefits in which the State will participate from the current \$10.10 per hour to \$6.75 per hour. **The LAO does not provide any recommendations, but indicates that the Legislature should weigh the budgetary savings against the potential for negative impacts on recipients and providers if counties elect to reduce wages.**

Suspend State Participation in Increased Contract Costs for IHSS. Proposes to save \$42.7 million annually by maintaining State participation in wages and in health benefits at the level of funding in the 2004 Budget Act (12 counties negotiated contracts to increase IHSS service provider wages/benefits since the 2004 Budget Act). **The LAO does not provide any recommendations, but indicates that the Legislature should weigh the budgetary savings against the potential for negative impacts on recipients and providers if counties elect to reduce wages.**

Foster Care. Proposes \$2 billion for Child Welfare Services, including expanded implementation of a Standardized Safety Assessment System. Additionally, it proposes legislation to allow the State to pass on to counties a portion of future Federal penalties associated with non-compliance by California with the Federal Child and Family Services Review. **The LAO recommends: 1) enacting legislation requiring the California Department of Social Services (CDSS) to provide an annual report to the Legislature which shows where each county, based on total funding and caseload, stands in relation to the workload standards for Child Welfare Services; and 2) reducing the foster care administration budget by 6 percent to reflect CDSS's updated foster care caseload projects; and 3) reducing the proposed foster care budget by \$21.6 million because the caseload projections are overstated for children living in group homes, foster family agency-certified homes, and seriously emotionally disturbed children.**

Child Support Services. Proposes \$194.1 million General Funds for local agency administrative costs, approximately the same level of funding provided in FY 2004-05. **The LAO recommends adoption of legislation establishing a 20 percent cap on administrative expenditures and the reduction of funding for those counties that exceeded 25 percent of the total funding on administration in the prior year.**

Federal Child Support Automation Penalty. Proposes \$218 million State funding for payment of the Federal Fiscal Year (FFY) 2005 penalty and assumes that the Federal government will allow the State to defer payment of the FFY 2006 penalty until September 2006. This proposal will allow the State to continue operating the Child Support Program in FY 2005-06 without loss of the program's Federal share of funding

or jeopardizing TANF funds. Completion of the new California Child Support Automation System is expected to be finalized and fully functional on a statewide basis in September 2008, as required by the Federal government. **The LAO does not provide any recommendations.**

Naturalization Services. Eliminates the program for a savings of \$1.5 million in FY 2005-06 and annually thereafter, noting that the State Department of Education provides similar services. **The LAO does not provide any recommendations.**

Foster Care. The Governor's budget proposes \$2.2 billion for Child Welfare Services, including expanded implementation of a Standardized Safety Assessment System. Additionally, it proposes legislation to allow the State to pass on to counties a portion of future Federal penalties associated with non-compliance by California with the Federal Child and Family Services Review.

The LAO indicates that based on their analysis, the proposed foster care administrative budget for 2004-05 and 2005-06 is over-budgeted based on the department's own projections of caseload. **The LAO recommends reducing the FY 2005-06 funding for foster care administration by \$2.3 million to reflect lower caseload. Additionally, the LAO recommends a reduction of \$10 million for FY 2004-05 and \$20.8 million for FY 2005-06 based on lower caseload projections.**

Child Welfare Services. The LAO indicates that data used for projecting the permanent placement caseload for the CWS budget estimate includes approximately 5,000 children placed with non-related legal guardians by the probate court. Because these children are not at risk of abuse and/or neglect, they do not receive services from social workers and should not be included in caseload estimates. As a result, the LAO recommends that proposed expenditures for child welfare services be reduced by \$4.8 million and suggests that the savings could be used to improve SB 2030 workload standards.

Child Support Services. Proposes \$194.1 million General Funds for local agency administrative costs, approximately the same level of funding provided in FY 2004-05. **Taking note of some counties' large administrative costs, the LAO recommends prospectively phasing in a 20 percent cap on administrative expenditures and a 25 percent cap for FY 2005-06 which would result in over \$6 million in savings.** The Administration further proposes to transfer \$79 million from DCSS to the Franchise Tax Board for the continued development of the Child Support Enforcement component of the Child Support Automation System project. **The LAO is withholding recommendation on this proposed transfer.**

Federal Child Support Automation Penalty. Perhaps, because it occurred so recently, the LAO did not address the denial by the Federal government of the Administration's request to defer the FFY 2006 penalty until the State's next fiscal

year, which will result in additional costs of \$167 million not provided for in the Governor's Budget.

General Government

SB 90 State Mandated Local Programs. Since deferral of local government reimbursement is no longer an option because of Proposition 1-A, the Administration proposes to suspend most mandates for a savings of \$250 million. The State would have no obligation to reimburse local governments that maintain the programs. In addition, the Administration proposes repayment of currently deferred amounts over a period of up to 15 years, rather than 5 years. The State currently owes the County over \$200 million.

In the "Perspectives and Issues" report, the LAO raises two significant issues for legislative consideration: 1) funding for Local Agency FY 2005-06 Mandates that are not suspended is insufficient by about \$67 million; 2) Proposition 1A seems to require the State to fund its mandate liabilities to local agencies for FY 2004-05 in the FY 2005-06 budget, which the Proposed Budget does not do, resulting in a shortfall of \$62 million.

Overall, the LAO points out that the Administration's proposals to suspend, revise or defer funding for mandates relating to significant programs lack explanation and the Administration fails to provide adequate information regarding its proposals which make legislative oversight difficult. Finally, the LAO recommends full funding for Health Benefits for Survivors of Peace Officers and Firefighters, which the Budget only partially funds, changing the Rape Victim Counseling Center Notice and Domestic Violence Information to statements of Legislative intent rather than funded mandates, and withholds judgment on the Open Meeting Act and Mandate Reimbursement Process mandates pending a proposal from the Administration.

Property Tax Grant Program. The Governor's Budget proposes a \$5.7 million reduction statewide to this program which will result in an estimated \$1.4 million loss to the County. **The LAO does not provide any recommendation.**

Los Angeles County Detection and Trapping. Includes an augmentation of \$760,000 for full year funding of staff for containment and eradication of fruit flies and pests. **The LAO does not provide any comments on this recommendation.**

California State Library. Proposes \$71.6 million, a \$3.3 million General Fund reduction from FY 2004-05. Reductions include \$2.2 million from the Public Library Foundation program, \$.83 million from the Library Development Program, and \$.27 million from the English Acquisition Program, for a total \$3.3 million General Fund reduction in local assistance. According to the County Librarian, the County's share of

the reduction will be \$220,000. **The LAO does not provide any comments on this recommendation.**

Natural Resources and Environmental Protection

Natural Resources. Includes \$164.7 million in local assistance funding from Proposition 50 and Proposition 13 bond funds to fund projects that improve water quality. **The LAO recommends that the Administration report at budget hearings on the status of the expenditure of resources bond funds appropriated in current and prior years.**

Environmental Protection. Increases appropriations for the Air Resources Board by \$69.6 million, including \$30.5 million for the full-year funding for the Carl Moyer Program authorized in FY 2004-05, and a \$25 million increase to provide additional mobile source emissions mitigation grants to local air districts. Reduces overall funding to the State Water Resources Control Board by \$305 million with most of the decrease due to less bond money being available in FY 2005-06. **The LAO recommends that departments continue to refine existing indicators so as to permit more precision in evaluating environmental outcomes of a particular program investment.**

Justice and Public Safety

Juvenile Justice Crime Prevention Act. Eliminates current year grant funding of \$100 million, but shifts \$25 million to the Board of Corrections for negotiations with counties on assuming increased responsibility for a number of changes in the juvenile justice system the Administration is proposing. The County currently receives \$28 million in grants, but would not be impacted until the next budget year because the program is funded a year in advance. **The LAO did not make a recommendation.**

Probation TANF Funding. Provided \$201.4 million in Federal TANF funding for juvenile probation services. TANF funds had been deleted from this program for the current year. **The LAO indicates that the use of TANF funds to offset General Fund costs for juvenile probation is feasible but it is a fiscal and policy decision for the Legislature.**

Youthful Offenders Parole Responsibility. Due to a projected decline in California Youth Authority (CYA) parolees, the Administration is proposing to shift supervisory responsibility from the CYA to counties. The parole population, which is projected to be 3,790 by June 30, 2005, is expected to decrease by 340 cases to 3,450 by June 30, 2006. Details of the plan and associated funding needs will be in the May Revision. **The LAO observes that details are lacking, but that the Administration will propose significant policy changes in the Youth Authority in the May Revision, including a potential shift of Youth Authority population and services to the local level.**

Judicial

Trial Court Funding. Increases funding by \$220.4 million to \$2.7 billion, due primarily to the restoration of a one-time reduction, a baseline budget adjustment, and a growth factor augmentation. In addition, there is a proposed transfer of \$14 million from Judicial to Trial Court funding for trial court operations. **The LAO withholds its recommendation on the proposed budget pending a report by the Judicial Council on its proposal to establish Uniform Civil Fees, especially the estimated revenues in the budget year.**

Undesignated Trial Court Fees. The Governor's Proposed Budget assumes the reauthorization of the transfer of \$29 million of undesignated trial court fee revenue from counties to the State trial court system. This transfer, which was agreed to by counties as part of the FY 2003-04 budget, was supposed to be for no more than two years and is scheduled to sunset at the end of this fiscal year. The County's share of the existing \$31 million transfer is \$9.8 million.

The LAO believes the proposed reauthorization of the undesignated fees transfer has merit to the extent the courts bear the costs of providing the services for which the fees are being collected. However, the LAO withholds its recommendation pending a revenue estimate for the Uniform Civil Fee proposal.

Transportation

Proposition 42. Proposes to suspend for two years the transfer of \$1.3 billion in sales tax revenue for transportation to be repaid over 15 years, including \$253 million to cities and counties that will impact street repaving in the unincorporated areas. **The LAO recommends that the administration provide information to the Legislature by April 1, 2005, to clarify the proposal's impact on the transportation program, especially the Traffic Congestion Relief Program. In the "Perspectives and Issues" report earlier this week, the LAO suggests that the Legislature consider repealing Proposition 42 and replacing it with a six cent gas tax increase, dedicated to transportation and indexed in future years.**

Pension Hearings

The Senate Budget and Fiscal Review Subcommittee #4 on State Administration held a lengthy hearing today to explore the budget implications of defined benefit versus defined contribution retirement plans. Joining subcommittee members Dunn, Kehoe, and McClintock were Senators Bowen and Soto.

Director of Finance, Tom Campbell, conveyed the Governor's concern that taxpayers should not be at risk if pension system investments go bad, and emphasized that, as long as the Governor's fundamental concern is addressed, there are a range of options

that can be discussed including an approach other than defined contribution plans, so long as the Legislature addresses the concern about not laying off risk onto the taxpayer.

Senators Joe Dunn and Debra Bowen expressed a desire to see implementing legislation reflecting the Governor's proposal before Assembly Member Keith Richman's constitutional amendment proposal is moved legislatively. Senator Bowen raised, at several points, a concern that women would be especially hard hit by a switch to defined contribution, since their average longevity is some 7+ years greater than men.

While some witnesses emphasized that a state decision would have a substantial impact upon local governments, others recommended the need for some degree of flexibility for employees, the need to look at the actuarial bases of defined benefit and defined contribution decisions over time, and the need to allow public employees help determine the outcome of reform.

Additional hearings will continue at later dates.

We will continue to keep you advised.

DEJ:GK
MAL:JF:JR:ib

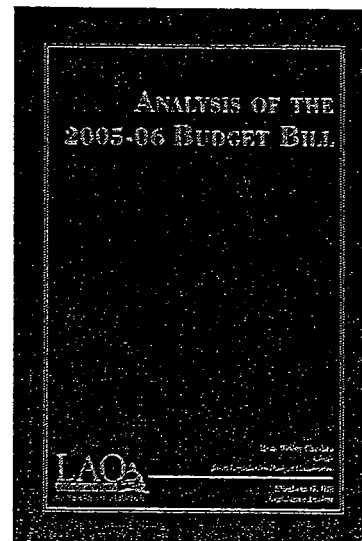
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February 24, 2005

Highlights of the 2005-06 Analysis

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Acknowledgments

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K-12 EDUCATION

➤ **Proposition 98—Governor Proposes \$2.9 Billion Increase**

- The budget proposes to leave 2004-05 Proposition 98 appropriations at roughly the level provided in the 2004-05 *Budget Act*. This proposal would create \$2.3 billion in General Fund savings over the two years. While the Governor's 2005-06 spending plan for K-14 grows by \$2.9 billion, it does not include funding to cover all K-14 operating expenses that districts would incur under the budget proposal.
- We recommend the Legislature build a base budget for 2005-06 that fully funds the current K-14 education program. (*Analysis*, page E-13.)

➤ **State Teachers' Retirement System (STRS) Proposal Lacks Benefits**

- The Governor proposes to shift financial responsibility from the state to K-14 education for \$469 million in annual contributions to STRS. The proposal, however, may not achieve the intended short-term goal of budgetary savings and does not resolve the longer-term issues with the current plan. (*Analysis*, page E-28.)

➤ **Some School Districts Face Difficult Fiscal Conditions**

- Some school districts face huge fiscal liabilities to pay for retiree health benefits. It will be difficult for districts to deal with these obligations without a long-term strategy. We recommend the Legislature take various actions to start addressing this problem. (*Analysis*, page E-47.)
- Around 40 percent of school districts face declining enrollment. The state continues to have inequities in revenue limit (general purpose) funding across school districts. We recommend an approach to address both of the problems, allowing declining enrollment districts to increase their per pupil revenue limit until they reach the equalization target. (*Analysis*, page E-53.)

➤ **Proposition 49—Recommend Repeal**

- We recommend the Legislature enact legislation placing before the voters a repeal of Proposition 49 because (1) it triggers an autopilot augmentation even though the state is facing a structural budget gap of billions of dollars, (2) the additional spending on after school programs is a lower budget priority than protecting districts' base education program, and (3) existing state and federal after school funds are going unused. (*Analysis*, page E-103.)

HIGHER EDUCATION

➤ **Governor Proposes to Put Universities' Budgets on "Autopilot"**

- The Governor's budget for the University of California (UC) and the California State University (CSU) follows the "compact" he developed with the segments last spring. The compact lays out annual targets for enrollment growth, fee increases, General Fund base increases, and other factors through 2010-11. By mapping out these funding choices up to six years ahead of time, the Governor's compact attempts to put the higher education budget on autopilot.
- We recommend the Legislature disregard the compact, and instead consider its various funding choices annually in the context of what is needed to achieve the state's higher education goals as expressed in the Master Plan. (*Analysis*, page E-149.)

➤ **Enrollment Growth Funding Should Be Based on Anticipated Demand**

- The Governor's budget includes funding for enrollment growth of 2.5 percent at UC and CSU, and 3 percent at California Community Colleges (CCC). The budget makes no attempt to link these growth rates to anticipated demand under the Master Plan.
- We recommend the Legislature fund enrollment increases of 2 percent at UC and CSU, and 1.9 percent at CCC. These recommendations are based on our estimates of increased enrollment demand in 2005-06. Implementing these recommendations would free up state funding for other priorities. (*Analysis*, page E-164.)

➤ **Budget Should Account for New Fee Revenue**

- The Governor's budget does not account for \$190 million in new student fee revenue that would result from planned fee increases at UC and CSU. Instead, he proposes that use of the resulting revenue be left entirely to the discretion of the segments.
- We recommend the Legislature include this anticipated fee revenue as part of its budget plan. Traditionally, fee revenue is used interchangeably with General Fund support to fund the segments' base programs. Taking this approach, the Legislature would be able to fully fund anticipated growth and inflation-driven increases, while freeing up some General Fund monies relative to the Governor's proposal. (*Analysis*, page E-192.)

- We also recommend the Legislature increase community college fees from \$26 per unit to \$33 per unit. This would raise about \$100 million in new fee revenue that could be used to fund legislative priorities. It would also leverage about \$50 million in federal funds to reimburse middle-income families for the higher fees. Financially needy students are exempt from paying fees at community colleges. (*Analysis*, page E-195.)

HEALTH SERVICES

➤ **Summary of Health Program Savings and Revenues**

- About \$294 million in Medi-Cal revenues from so-called “quality improvement fees” have not been counted as state revenues in the Governor’s budget. We recommend the Legislature recognize these fee revenues as it drafts its budget plan. (*Analysis*, page C-66.)
- We also identify the potential for an additional \$100 million net gain to the state from establishing such fees for hospitals. (*Analysis*, page C-100.)
- In addition, we identify more than \$190 million in potential expenditure reductions. (*Analysis*, pages C-105, C-138, C-142, C-143, C-157, C-162, and C-178.)

➤ **Part “D” Stands for “Deficit”:**

How the Medicare Drug Benefit Affects Medi-Cal

- Part D of the federal Medicare Modernization Act establishes a prescription drug benefit for Medicare recipients and in so doing has major implications for the Medi-Cal Program. It is likely to result in significant net costs to Medi-Cal beyond the budget year. (*Analysis*, page C-105.)

➤ **Medi-Cal Redesign Sound in Principle But Needs Further Development**

- The seven-part administration redesign proposal would result in broad changes in Medi-Cal managed care as well as some more limited changes in benefits, cost-sharing, and eligibility administration. Overall, we find that the Governor’s proposals are conceptually sound but that the Legislature needs more information about some aspects of the package and that some refinements are warranted. (*Analysis*, page C-67.)

➤ **Hospital Financing Plan Could Begin to Right Ailing System**

- The state's hospital system continues to face a variety of fiscal challenges that weigh particularly heavily on public hospitals. The administration is negotiating with the federal government for a comprehensive redesign of hospital financing as part of its Medi-Cal redesign package. Our review of the plan now under development suggests that it could help preserve the financial stability of public hospitals but also raises some significant fiscal and policy issues. (*Analysis*, page C-83.)

➤ **Towards a More Systematic Rate-Setting Model for Regional Centers**

- Our analysis finds that the way the state sets rates for vendors who provide community services for the developmentally disabled on the whole lacks a rational and consistent approach. We review how rates are set for these services and offer an improved and systematic approach that could achieve significant state savings. (*Analysis*, page C-167.)

➤ **Proposition 63 Language Requires Clarification**

- In November, California voters approved Proposition 63, a measure imposing a new state income tax surcharge to expand community mental health systems. We recommend the enactment of legislation that would clarify the meaning of some key but ambiguous provisions of the measure in order to ensure its smooth and effective implementation and avoid future state budget problems. (*Analysis*, page C-182.)

➤ **Proposition 99: Too Many Programs, Too Few Dollars**

- We recommend the Legislature approve the Governor's budget proposal for Proposition 99-funded programs, which shifts allocations of tobacco tax revenues to maximize resources for health programs and achieve General Fund savings. We further recommend that the Legislature begin this year to address the long-term issues posed by the present structure of Proposition 99. (*Analysis*, page C-129.)

➤ **Accessing Federal Funds for Prenatal Services**

- We recommend approval of the Governor's proposal to draw down federal funds to offset state costs for prenatal services but examine the idea of expanding this option to also reduce the state cost of providing these services to incarcerated women. We further recommend enactment of

legislation to consolidate the Access for Infants and Mothers Program into the Healthy Families Program. (*Analysis*, page C-19.)

➤ **Antiobesity Initiative Should Itself Be Slimmed Down**

- While additional state public health efforts to combat the spread of obesity are warranted, the Governor's proposal launches new antiobesity projects before an assessment of existing efforts has been completed. It also does not take advantage of alternative funding sources available to the state. We recommend reducing the funding and staff requested for the projects. (*Analysis*, page C-138.)

➤ **Evaluating the Administration's California Rx Proposal**

- The Governor's 2005-06 budget plan includes a funding request and related legislation for a new state program to help low- and moderate-income Californians purchase prescription drugs at discounted prices. Our analysis indicates that the Governor's plan for drug discounts for the uninsured provides a reasonable starting point for the development of such a program. However, we propose, among other changes, that in the event that drug makers fail to make good on their promises for significant price concessions, an automatic trigger would phase out the proposed voluntary approach, and be replaced by an alternative strategy likely to result in greater discounts on more drugs for consumers. (*P&I*, "Part V.")

SOCIAL SERVICES

➤ **Substantial Progress in Reducing Social Worker Caseloads**

- In 2000, a legislatively mandated study found that it was difficult for social workers to provide services or maintain meaningful contact with children and their families because of the large numbers of cases they were expected to carry. Our analysis indicates California now meets or is approaching the three of the five workload standards in child welfare services. We recommend enactment of legislation requiring the administration to report annually on county-specific social worker staffing ratios so that the Legislature remains informed about progress in this area. (*Analysis*, page C-214.)

➤ **Reducing the Earned Income Disregard**

- Effective October 2005, the Governor proposes to lower the grants for all working California Work Opportunity and Responsibility to Kids recipients,

by reducing the amount of earned income which is disregarded (not counted) when determining a family's grant. This proposal results in savings of \$80 million and is likely to have minimal impact on the work incentive. We present alternative approaches which are likely to increase the work incentive but result in less budgetary savings. (*Analysis*, page C-214.)

➤ **Social Services Reductions Represent Substantial Ongoing Budget Solution**

- The Governor proposes to reduce social services expenditures by \$1.1 billion (in comparison to the requirements of current law). Social services expenditures represent just under 11 percent of the total General Fund budget while the reductions account for about 20 percent of the proposed budget solution excluding borrowing. The Legislature faces difficult choices in the area of social services because rejection of any the social services reductions will require making ongoing reductions in other programs or increases in revenues.

➤ **Child Care Reforms Merit Serious Consideration**

- The Governor proposes a number of significant reforms to California's subsidized child care system including eligibility restrictions, a new waiting list system, and tiered reimbursement rates. With certain qualifications, we support proposed eligibility and waiting list changes. Although tying reimbursement rates to quality makes sense, the Legislature may wish to consider alternative approaches which increase reimbursement rates for higher quality care rather than simply reducing reimbursement rates (as the Governor proposes) for lower quality care. (*Analysis*, page C-25.)

➤ **Social Services Programs Overbudgeted by \$180 Million**

- Our review of various social services programs identifies a series of overstated caseloads and estimating errors. We find that for 2004-05 and 2005-06, the budget overstates social services costs by almost \$180 million and we recommend that the Legislature score corresponding savings. (*Analysis*, pages C-206, C-212, C-232, C-241, and C-244.)

➤ **Other LAO Saving Recommendations**

- In addition to the almost \$180 million in caseload and estimating savings described above, we make recommendations in Foster Care, Child Support, and the Employment Development Department resulting in other General Fund savings totaling \$12 million. (*Analysis*, pages C-197, C-243, and F-92.)

CORRECTIONS

➤ **CDC Disciplinary Confinement Practices Need Improvement**

- As a means of controlling prison violence, California Department of Corrections (CDC) has established several “disciplinary confinement” options, including administrative segregation and special housing units. Despite increasing use of such options, data show inmate assaults (and the associated state costs) continue to increase. Our examination identifies a number of shortcomings in the department’s disciplinary confinement policies and practices, and offers recommendations for improvement. Depending on the recommendations adopted, savings could be up to \$10 million in 2005-06. (*Analysis*, page D-34.)

➤ **Court Requires Further Improvements in Inmate Health Care**

- In September 2004, a federal court issued an order requiring further improvements in CDC’s inmate health care delivery system. We recommend a number of modifications to the Governor’s budget proposal that would result in state General Fund savings, while allowing the state to comply with the court order. (*Analysis*, page D-52.)

➤ **State Could Save More on Foreign Prisoner Transfers**

- The Foreign Prisoner Treaty Transfer program has the potential to reduce state incarceration costs by transferring inmates to their country of origin. Because of administrative issues, the state does not obtain the maximum benefit that could be achieved from this program. We offer recommendations for increasing the program’s use and state savings. (*Analysis*, page D-19.)

➤ **Ward Population Continues to Decline, More Closures Proposed**

- The Youth Authority projects the ward population to drop 12 percent (465 wards) by June 2006, and to further decline to just over 3,000 by June 2009. The Governor’s budget proposes to close two youth conservation camps at the end of the current year. Given the continuing drop in the ward population, and the low number of wards who qualify to participate in the camp program, we think the proposed closure is prudent. However, we think the administration should report on its plans to convert these camps to adult inmate camps. (*Analysis*, page D-67.)

➤ **Proposition 69 (DNA) Request Overbudgeted**

- The Governor's budget includes funds for implementation of Proposition 69—DNA Collection—by the Departments of Justice, Corrections, and Youth Authority. While these departments will require funding to collect and process tens of thousands of additional DNA samples in 2005-06, our analysis indicates that the requests for Corrections and Youth Authority are overbudgeted by \$3.5 million. (*Analysis*, page D-13.)

➤ **Up to \$65 Million in General Fund Savings Identified**

- In our review of the Governor's budget, we recommend a number of actions that would result in up to \$65 million savings in 2005-06, mostly in CDC's budget. This level of savings would primarily be achieved by reducing budget requests that are overbudgeted or that lacked sufficient justification. (*Analysis*, pages D-13, D-19, D-30, D-34, D-46, D-48, and D-52.)

➤ **Assessing the Governor's Reorganization Proposals**

- On January 6, 2005, the administration released its plans to eliminate 88 boards and commissions and to reorganize the Youth and Adult Correctional Agency (YACA). For each of the plans, we provide an assessment of its fiscal effect and raise key issues. Although the administration recently has decided not to forward its boards and commissions proposal to the Legislature, the piece provides key considerations for the Legislature when seeking to consolidate these types of entities. Regarding the YACA proposal, we conclude it has the potential to improve the efficiency, accountability, and effectiveness of the state's prison system. However, the plan omits important details that the Legislature requires in order to fully evaluate its merits. Our analysis indicates that the proposed reorganization would probably result in net costs in the short term, but has the potential to achieve significant long-term net savings by placing a greater emphasis on inmate rehabilitation as a means of increasing public safety. (*P&I*, "Part V.")

CAPITAL OUTLAY

➤ **Administration Did Not Submit Statewide Infrastructure Plan**

- The administration did not submit a statutorily required infrastructure plan that identifies (1) the statewide infrastructure improvements to be funded over the next five years and (2) the funding sources for these improvements. Without the plan, the Legislature has no information about the

administration's priorities regarding infrastructure investment. We recommend the Legislature defer action on all capital outlay proposals for new projects until the 2005 infrastructure plan is submitted. (*Analysis*, page G-15.)

➤ **Bond Funds Are Not Sufficient to Complete All Higher Education Projects**

- The budget proposes to use higher education bond funds to develop 17 projects that will require substantial funding to complete in future years. There are not sufficient bond funds remaining to cover all of the projects' future costs, and the availability of other state funds to complete the projects is uncertain. We recommend that the remaining bond funds be used to fund the completion of ten projects based on their priority ranking. We further recommend that funding to develop seven lower-priority projects be approved contingent upon the higher education segments committing to using nonstate funds to complete the projects if state funds are not available in the future. (*Analysis*, page G-34.)

TRANSPORTATION

➤ **Misleading Caltrans' Budget Display Weakens Legislative Oversight**

- It is impossible to determine Caltrans' total transportation expenditures because its budget display uses a mix of cash and accrual accounting. As a result, the Legislature is unable to ascertain the magnitude of Caltrans' project commitments or payments in any one year. We recommend the enactment of legislation requiring transportation expenditures to be displayed according to standard budget display requirements. (*Analysis*, page A-18.)

➤ **More Thorough Diagnosis of "Chief's Disease" Needed**

- Since 2000, more than three-fourths of California Highway Patrol's (CHP's) senior-ranking officers have retired due to work-related injuries (referred to as industrial disability retirement [IDR]). This compares to 60 percent of rank-and-file officers. The CHP cannot adequately explain the disparity between the IDR rates for senior officers and rank-and-file officers. We recommend the Legislature direct CHP to report on the nature of the problem—particularly the reasons for the difference in IDR rates among chiefs and lower-ranking uniformed staff—as well as ways to assess the effectiveness of the department's actions in addressing workers' compensation and IDR issues. (*Analysis*, page A-31.)

➤ **DMV Needs to Avoid Delays in Evaluating Unsafe Drivers**

- In 2003-04, the Department of Motor Vehicles (DMV) was able to complete within the 30-day statutory deadline only 8 percent of administrative hearings for drunk-driving cases. In addition, in that year it took an average of 42 days before DMV staff scheduled a "regular re-examination" of certain drivers who may not be physically or mentally able to safely operate a motor vehicle. Absent corrective actions at the department, delays in evaluating potentially unsafe drivers are likely to increase. We recommend the Legislature direct DMV to transfer certain workload involving high-risk drivers to the customer-service field offices in order to reduce these delays and to report on the impact of the transfer. (*Analysis*, page A-38.)

➤ **Transportation Funding Instability Continues**

- The administration proposes to suspend \$1.3 billion in Proposition 42 transportation funding and to reduce the General Fund's commitment to repay transportation loans in the near term. This would help the General Fund condition but restrict already limited transportation funding and increase near-term funding uncertainty. We recommend the administration provide information to clarify (1) the effect of the Governor's proposals on the size of the transportation program and (2) Traffic Congestion Relief Program funding requirements in 2005-06.
- The administration also proposes to prohibit the suspensions of Proposition 42 after 2006-07. This would increase transportation funding stability in the long run. However, this stability would be lessened by another administration proposal that General Fund expenditures, which include Proposition 42 funding, be cut across the board under certain circumstances. In order to provide long-term transportation funding stability while freeing up General Fund revenue for other purposes, we continue to recommend (1) the repeal of Proposition 42, (2) an increase of the gas tax to generate an amount of funding equivalent to Proposition 42, and (3) adjusting the gas tax for inflation. (*P&I*, "Part V.")

➤ **Toll Bridge Seismic Retrofit:
Hard Decisions Before the Legislature**

- The administration recently estimated the toll bridge seismic retrofit program requires an additional \$3.2 billion to complete and has recommended changing the Bay Bridge's design to save money. The Legislature faces two key decisions: (1) whether to approve a redesign of the Bay Bridge east

span and (2) how to fund the program's completion. Redesigning the Bay Bridge could save money, but also raises the risk of cost and schedule increases that could more than offset the savings. As regards the funding issue, we recommend that support be provided by both state and local sources. The Legislature has several options regarding the sources used and the amount to provide from each. (*P&I*, "Part V.")

RESOURCES

➤ **Should the State Issue Debt to Finance Flood Lawsuit Settlement?**

- The budget proposes to use a "judgment bond" to finance a pending \$464 million settlement of a lawsuit stemming from a major flood in Yuba County in 1986. We believe that there may be alternative ways to fund the state's obligation from the lawsuit. However, if the administration proceeds with its plan to finance the settlement with a judgment bond, there are a number of legal, policy, and fiscal issues for the Legislature to consider, including whether the proposed bond would require a vote of the people and how the bond should be structured to minimize its cost. We highlight these issues and recommend the Department of Finance report at budget hearings on them. (*Analysis*, page B-79.)

➤ **Reorganization of Energy-Related Agencies Raises Issues**

- The Governor's Reorganization Plan Number One proposes to eliminate two energy-related agencies—The California Consumer Power and Conservation Financing Authority and the Electricity Oversight Board—and transfer their responsibilities to the California Energy Commission. Although the administration recently decided not to forward this plan to the Legislature, the piece provides an assessment of issues related to such a reorganization. (*Analysis*, page B-27.)

➤ **Recycling Goals Could Be Met More Effectively and Efficiently**

- In order to more effectively and efficiently meet the state's recycling goals, we recommend that the recycling and related waste prevention programs in the Department of Conservation (DOC) and the California Integrated Waste Management Board (CIWMB) be consolidated into one department. In addition, we recommend the elimination of CIWMB and the transfer of its remaining responsibilities to an expanded Department of Toxic Substances Control, thereby generating \$2 million in special fund savings. Finally, we

recommend the Legislature consider options for transferring the remaining nonrecycling functions of DOC to existing state agencies. (*Analysis*, page B-17.)

➤ **Significant Amounts of Pesticide Fees Not Being Collected**

- The Governor's budget does not address an undercollection of the pesticide mill assessment (levied at the first point of sale of a pesticide in California) that has been identified in recent departmental audits of retailers of consumer (nonagricultural) pesticides. We offer options to improve the collection of the pesticide mill assessment and recommend that the administration report on these and other ways of addressing this issue at budget hearings. (*Analysis*, page B-85.)

➤ **Fire Protection Budget: Details Lacking, Oversight Difficult**

- The budget proposes \$10.8 million for new firefighting equipment and helicopters and \$9 million for year-round firefighting staffing in Southern California. We find that details and justification for these proposals are lacking and therefore recommend the Legislature deny the funding requests. (*Analysis*, page B-52.)
- It has been difficult for the Legislature to oversee the California Department of Forestry and Fire Protection's use of federal funds, which it receives after assisting the federal government at a fire. In some cases, these funds have been diverted to purposes other than fire protection. We make recommendations to improve legislative oversight over the department's receipt and use of these federal funds. (*Analysis*, page B-56.)

➤ **Water Policy Issues Facing the State**

- The state oversees about 1,600 miles of levees that are aging and deteriorating. Should these levees fail, the state would face a major liability. We analyze and make recommendations regarding the strategies proposed by the administration to address various flood management problems identified in a recent Department of Water Resources White Paper. Our recommended legislative steps include actions to evaluate the structural integrity of the state flood control system, enact a flood control benefit assessment, re-evaluate the state's role with respect to Delta levees, and reduce the likelihood of ill-advised development approvals in flood-prone areas.
- The CALFED Bay-Delta Program (CALFED) is at a funding crossroads given that its primary funding source in recent years—state bond funds—is running out at the same time as the program is projecting \$6.3 billion of unmet

funding requirements over the next ten years. The program's oversight agency—the California Bay-Delta Authority—has recently approved an \$8.1 billion ten-year finance plan for the program that assumes major new sources of federal funds, unidentified state funds, and water user fees. Given that some of the revenue assumptions underlying the plan appear unrealistic, the Legislature will need to establish its expenditure priorities for CALFED so that the program can be “right sized” consistent with those priorities. (*P&J*, “Part V.”)

GENERAL GOVERNMENT

➤ **State Needs Unified Strategic Approach to Homeland Security**

- The state lacks a unified strategic approach to homeland security. The Office of Homeland Security and the Department of Health Services have not sufficiently coordinated their efforts. We make a number of recommendations to address these problems, including the development of a strategic plan and annual expenditure report. (*Analysis*, page F-13.)

➤ **Governor's Data Center Consolidation Proposal Would Foreclose Legislative Oversight**

- The Governor proposes to consolidate the state's two largest data centers into the Department of Technology Services. A consolidated data center should ultimately result in improved services and reduced costs. A number of specific components of the proposal, however, would preempt the Legislature's appropriation and oversight roles. For instance, the department's expenditures would be controlled by administration officials outside the purview of the Legislature. Consequently, we recommend the Legislature approve the consolidation but modify some key components. (*Analysis*, page F-76.)

➤ **Doubling the Size of the Gambling Commission Not Justified**

- The budget proposes an augmentation of \$4.8 million and 46 two-year limited-term positions for increased regulatory activities related to tribal gambling. The request would double the size of the California Gambling Control Commission. The request fails to (1) clearly articulate what problems are being addressed, (2) justify a new state gaming lab, and (3) reflect a joint strategy with the Department of Justice. We recommend the Legislature reject the request and the administration resubmit a proposal which addresses these problems. (*Analysis*, page F-31.)

➤ **Federal Deadline for Voter Database Approaching**

- The implementation of the federal Help America Vote Act of 2002 (HAVA) represents a significant opportunity for the Legislature to upgrade the state's election systems and improve the administration of election laws. At a statewide level, the most pressing HAVA deadline is the requirement to have a federally compliant voter registration database operational by January 1, 2006. We offer a number of key considerations to assist the Legislature in implementing HAVA. (*Analysis*, page F-40.)

➤ **Addressing Public Pension Benefits and Cost Concerns**

- California "defined benefit" pensions in the public sector raise certain benefits and cost issues. For instance, some formulas provide retiree benefits that equal their working income. In addition, governments are "on the hook" for all increased retirement system costs. In response, the Governor proposes shifting all new public sector employees to "defined contribution" plans. Defined contribution plans address concerns with defined benefit pensions, but also introduce issues of their own. The Legislature could also address the benefits and cost concerns of current retirement plans within the existing defined benefit structure or with other pension plan alternatives. (*P&I*, "Part V.")

➤ **Lowering the State's Costs for Prescription Drugs**

- Our review of the state's \$4.2 billion annual purchases of prescription and nonprescription drugs found several deficiencies in the state's procurement process which lead to it paying higher prices than necessary. We offer a number of recommendations to correct these procurement and administrative problems that, if implemented, would generate savings totaling tens of millions of dollars annually. For example, we recommend a short-term fix of increasing collaboration between state drug purchasers in order to share more drug pricing information and a long-term fix of leveraging the Medi-Cal drug formulary to lower drug prices in non-Medi-Cal programs. (*P&I*, "Part V.")